

Before the
Federal Communications Commission
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)	
)	
Federal-State Joint Board on)	CC Docket No. 96-45
Universal Service)	
)	
1998 Biennial Regulatory Review – Streamlined)	CC Docket No. 98-171
Contributor Reporting Requirements Associated)	
With Administration of Telecommunications Relay)	
Service, North American Numbering Plan, Local)	
Number Portability, and Universal Service Support)	
Mechanisms)	
)	
Telecommunications Services for Individuals with)	CC Docket No. 90-571
Hearing and Speech Disabilities and the)	
Americans with Disabilities Act of 1990)	
)	
Administration of the North American Numbering)	CC Docket No. <u>92-237</u> /
Plan and North American Numbering Plan Cost)	NSD File No. L-00-72
Recovery Contribution Factor and Fund Size)	
)	
Numbering Resource Optimization)	CC Docket No. 99-200
)	
Telephone Number Portability)	CC Docket No. 95-116

REPLY COMMENTS OF THE
TEXAS OFFICE OF PUBLIC UTILITY COUNSEL
CONSUMER FEDERATION OF AMERICA
CONSUMERS UNION

July 9, 2001

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I. INTRODUCTION

The Texas Office of Public Utility Counsel, the Consumer Federation of America and Consumers Union (hereafter Consumer Commenters) appreciate the opportunity to file reply comments in response to the Notice of Proposed Rulemaking.¹ We are gratified to find that the overwhelming majority of commenters in this proceeding agree with our initial comments. They urge the Federal Communications Commission (hereafter the Commission or the FCC) to reject the idea of moving to a fixed, per line charge to assess and/or recover contributions to the universal service fund.

The large business customers² and the Interexchange Carriers (IXCs)³ are the primary parties pressing for a major change in the system for funding universal service support. This pattern is easily explained and mirrors their frequent interventions before the Commission.

The large business customers, who are by far the heaviest users of the interstate telephone network, seek to shift the cost burden of the network to residential and small business customers, thereby lowering their share of universal service payments. The interexchange carriers (IXCs) blame their inability to compete effectively on Commission rules and seek to evade their responsibility to make a contribution to universal service. Both

¹ "Initial Comments of the Texas Office of Public Utility Counsel, the Consumer Federation of America and Consumers Union," In the Matter of Federal-State Joint Board on Universal Service, 1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated With Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms, Telecommunications Services for Individuals with Hearing and Speech Disabilities and the Americans with Disabilities Act of 1990, Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size, Numbering Resource Optimization, Telephone Number Portability, CC Docket Nos. 96-45CC, 98-171, 90-571, 92-237CC, 99-200CC, 95-116, and NSD File No. L-00-72, June 25, 2001. All subsequent citations are to the initial comments filed in this proceeding.

² "Comments of the Ad Hoc Telecommunications Users Committee" (hereafter, Ad Hoc).

³ "Comments of AT&T" (hereafter, AT&T); "Comments of Sprint" (hereafter, Sprint); "Comments of Worldcom, Inc." (hereafter, Worldcom).

recommend that residential and small business customers pay an inflated, fixed charge far out of proportion to their usage of the network. Both seek to mask their blatantly self-serving arguments in claims of competitive neutrality or economic and/or administrative efficiency.

In contrast, in a rare show of consensus, consumer interveners,⁴ local exchange companies (ILECs)⁵ and their trade associations,⁶ as well as network administrators⁷ and numerous other industry participants⁸ agree that basing universal service contribution on per-line or per-account charges is inequitable⁹ and illegal.¹⁰ They agree that the calculation of contributions to the universal service fund should be based on revenue or usage.¹¹ They recommend that, to the extent an interexchange carrier chooses to recover those contributions

⁴ In addition to Consumer Commenters see “Initial Comments of the West Virginia Consumer Advocate” (hereafter, West Virginia); “Initial Comments of the National Association of State Utility Consumer Advocates” (hereafter, NASUCA); “Comments of Center for Digital Democracy, Edgemont Neighborhood Coalition and Migrant Legal Action Program” (hereafter, CDT), address only the issue of universal service charges for dial-around services and their recommendations are consistent with the recommendations made by other consumer advocates in the broader program.

⁵ “Comments of SBC Communications Inc.” (hereafter, SBC); “Comments of Verizon,” (hereafter, Verizon); “Comments of Qwest Communications International, Inc.” (hereafter, Qwest); “Comments of Bell South (hereafter BST).

⁶ “Comments of the United States Telecom Association” (hereafter, USTA); “National Telephone Cooperative Association Initial Comments,” (hereafter, NTCA); “Comments of the Organization for the Promotion and Advancement of Small Telecommunications Companies,” (hereafter, OPASTCO); “Comments of the American Public Communications Council” (hereafter, APCC); “Comments of the Association of Communications Enterprises” (hereafter ASCENT).

⁷ “Comments of the Universal Service Administrative Company” (hereafter, USAC); “Comments of the National Exchange Carrier Associations, Inc.” (hereafter, NECA); “Comments of the Iowa Utilities Board” (hereafter IUB).

⁸ “Initial Comments on Behalf of IDT Corporation” (hereafter IDT); “Comments of Home Telephone Company” (hereafter Home); “Comments of BT North America Inc.” (hereafter BTNA); “Comments of Brown University” (hereafter Brown); “Comments of Time Warner Telecom” (hereafter TWT); “Comment of EPIK Communications Incorporated” (hereafter EPIK).

⁹ OPASTCO, p. 5; BST, p.3; Verizon, p. 5; APCC, p. 3.; ASCENT, p. 5; NECA, pp. 3,6; Home, p. 5; BTNA, p. 10.

¹⁰ NCTA, p.2; BST, p. 2; Qwest, pp. 8—9; Verizon, pp. 2-4; USTA, p. 5.

¹¹ Qwest, pp. 3-5, 12; SBC, p. 4; West Virginia, p. 2; USTA, p. 4; IUB, p. 2; CTCA, p. 1; OPASTCO, p. 2; NECA, pp. 2,6; TWT, p. 2; Home pp. 3,6.

in a line item on the bill, it be limited to a uniform percentage of revenue or usage basis.¹² There is virtually unanimous support for the exemption of lifeline customers from universal service payments, should the Commission allow line items to be placed on the bill.

The Commission must see the special pleading of the large business customers and IXC's for what it is, an effort to avoid shouldering a fair share of the burden of maintaining universal service. While some of the problems that the large business customers and IXC's identify with the current system must be addressed, their solution moves in exactly the wrong direction.

Therefore, based on the record in this proceeding, the Commission should

(1) Fine tune the revenue-based allocation of universal service obligations by adjusting obligations on a quarterly basis. This will respond to complaints by IXC's that the lag in calculating their obligation places them at a competitive disadvantage.

(2) Expand the base of contributions to universal service to ensure that all interLATA traffic contributes equitably to the promotion and maintenance of universal service. It must revisit the wireless safe harbor. It must commence a proceeding to consider how the telecommunications services supporting Internet-bound traffic, which is now fully in the federal jurisdiction, can make an equitable contribution to universal service.

¹² SBC, p. 7; APCC, p. 2; IUB, p. 3; Brown, p. 3; Home, p. 7; CDD, pp. 6-7, supports this as an option to disallowing line items altogether for dial-around service providers.

(3) Reform the practice of placing universal service charges at the bottom of the bill by either eliminating them or requiring that they be a uniform percentage of the bill.

II. BROADLY SUPPORTED REFORM IN THE SYSTEM FOR FUNDING UNIVERSAL SERVICE

A. Eliminating Bottom of the Bill Charges for Universal Service Cost Recovery

The consumer interveners and others generally agree that any shift to a per line recovery of universal service fund costs is unwarranted, if not illegal. They support continuation of a usage or revenue basis for calculation of carrier obligations and the removal of any line item to recover these costs from consumers. They argue that universal service funds should be treated as every other cost of business and recovered in the general rates charged by long distance companies.

Eliminating the line item will reduce by one the bottom of the bill charges that make deception and confusion inevitable in the long distance market.¹³ These commenters point out that the IXC's have repeatedly and continuously failed to inform consumers of their bottom of the bill charges in advertising, which misleads the public about the cost of service. Making the charge uniform does not overcome the fundamental deception.

We support this point of view and believe the only way to prevent the industry from continuing to mislead the public is to preclude them from using bottom of the bill charges to recover these costs.

¹³ NASUCA, pp. 8-9; West Virginia, p. 5; CDD, pp. 6-7.

B. Line Items Are Illegal.

In our initial comments, we demonstrated that line items violate the clear language of the statute that requires interexchange carriers to contribute to universal service.¹⁴ Numerous commenters raise another legal barrier to per line or per account charges.¹⁵ They maintain that this violates the 5th Circuit Appeals Court ruling that contributions to universal service be based only on interLATA services.

In fact, the way the IXC's frame the problem, they all but invite a lawsuit over a per line or per account charge. Worldcom's discussion can serve as an example. First it argues that changes in the industry "will make it increasingly difficult to distinguish between interstate and intrastate services."¹⁶ Then it portrays the line item as an approach that does not make such a distinction because "using the connection- and capacity-based approach will eliminate the need for providers of bundled services to estimate the portion of revenues generated that is attributable to interstate telecommunications services."¹⁷

While the Court's interpretation was controversial, and the continuing developments of bundled services may make it necessary to revisit the court's interpretation either legally or legislatively, for the moment, the ILEC's legal argument is persuasive. Because the IXC's proposal does not distinguish nor justify the surcharge based on services and revenues solely within the federal jurisdiction, that proposal to collect flat rated line charges or account

¹⁴ Section 254 (b)(4)

All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.

¹⁵ NCTA, p.2; BST, p. 2; Qwest, pp. 8—9; Verizon, pp. 2-4; USTA, p. 5; NTCA, p. 2.

¹⁶ Worldcom, p. 14.

¹⁷ *Id.*, p. 19.

charges fails to follow the Court's ruling to exclude intrastate revenues and services from the collection of federal USF support.

C. Expand the Base of the Fund

There is one area where the large business/IXC commenters make a positive contribution to the proceeding.¹⁸ In this they join most other parties in making a good case that the base of the universal service fund must be expanded.¹⁹

The Commission has already identified wireless traffic as a potential source of contribution to the universal service fund. It created a safe harbor on the basis of an assumption that the use of wireless is similar to that of wireline. Since the Commission adopted that rule, the extent and nature of wireless usage has changed dramatically. The number of wireless users has expanded dramatically in part because pricing patterns have changed with the offer of bundles of minutes at a fixed price. This encourages interLATA usage.

While it may be difficult for individual wireless companies to identify interLATA usage on an ongoing basis, many do identify calls even for billing purposes, even in their bundles. At a minimum, the FCC should study the pattern of wireless usage that has developed since the rule and adjust its safe harbor appropriately. It should investigate the extent to which wireless carriers record minutes of use by origin and destination, even for packages of minutes, as a basis for determining the amount of interLATA traffic handled by

¹⁸ Worldcom, p. 12; Sprint, p. 13, Ad Hoc, pp. 16, 30; NTCA, p. 4.

¹⁹ Verizon, p. 5; SBC, pp. 4, 10-13; USTA, p. 7; NCTA, p. 4, IUB, p. 12; NECA, p. 7.

wireless carriers.²⁰ Of course, wireless carriers object to revisiting the safe harbor that set a low level of contribution to universal service.²¹

III. INCORRECT OR MISLEADING JUSTIFICATIONS FOR PER LINE UNIVERSAL SERVICE FUND CHARGES

The above modification will strengthen the universal service funding mechanism, make it more equitable and less confusing. The arguments offered for a radical shift to a per line charge do not stand close scrutiny.

A. Competitive Neutrality is a Cover for Competitive Ineptitude.

AT&T claims that recovery of costs on a percentage of revenue basis places it at "risk of non-recovery of costs."²² Similarly MCI claims that incumbent long distance carriers are placed a disadvantage because new entrants will always pay less for universal service than they should as their business is growing.²³

What both of these arguments say is that the incumbents cannot or do not wish to compete. Because some IXCs cannot preserve their share of a rapidly growing market, using historical market shares overcharges them.

²⁰ Home, p. 8, suggests an annual update of the safe harbor.

²¹ "Comments of Tellstar;" "Comments of Arch Wireless, Inc.;" "Comments of AT&T Wireless Services, Inc.;" "Comments of Verizon Wireless;" Comments of the Rural Cellular Association;" "Comments of the Cellular Telecommunications & Internet Association." "Comments of Nextel Communications, Inc." support a flat fee, or preservation of the current safe harbor.

²² ATT, pp. 2, 3, 4.

²³ Worldcom, p. 15.

In fact, there is just as much chance that there will be an over recovery of costs with the current system by those who are winning larger market shares. The regulatory approach is perfectly balanced. The problem is that some companies want to be protected from the competitive market.

Exhibit 1 shows the growth of toll revenues for long distance companies since the passage of the 1996 Act. Total revenues have increased by almost one-third, but AT&T's revenues have been flat. Because it cannot compete, its share of the revenue pie has declined sharply.

Worldcom's share of the revenue pie has declined slightly. Since it cannot point to a significant past problem, it predicts that long distance revenues will soon decline and, since it cannot compete, it will suffer a declining share of future revenues.²⁴ Sprint's share has increased, so it does not make the argument that it is systematically disadvantaged by the revenue methodology.

In all circumstances, the recent move to a six-month reporting period will reduce AT&T's past problem and Worldcom's prospective problem of paying too much because they cannot compete. A further move to adjust recovery on a quarterly basis would further shrink the lag and relieve the shrinking firms of any regulatory induced disadvantage. However, the Commission should reject the argument that there is a systematic problem with basing contributions on a percentage of revenue basis. Universal service costs are like any other costs. If you win in the market, you will recover your costs. If you do not, you will not.

B. Claims of Simplicity in Per Line Charges are Based on Arbitrary Assumptions.

Any simplicity that is accomplished by the proposed per line or per account charge is a function of arbitrary, unjustified decisions and failure to resolve critical issues.²⁵ To the extent the Commission is given guidance, it is arbitrary. Worldcom picks arbitrary numbers for recovery of costs. It punts altogether on how universal service burden will be allocated and recovered on a line that is shared between IXC and data CLEC. In their approach, either the interLATA voice or the interLATA data usage will not make a contribution to universal service. In our approach, which bases contribution on revenues or minutes of use, both will make a contribution that is proportionate to their use of the network.

Sprint's proposal is equally arbitrary.²⁶ Sprint presents a series of black box allocators that will have to be developed by the Commission as a future time.

C. Treating Universal Service as a Head Tax is Unjustified and Contrary to the Act

In our initial comments, Consumer Commenters articulated a view of universal service that argued that usage of the network was the best indicator of how benefits are derived from the ubiquity of the network. We pointed out that actual use of the network must be one of the cornerstones of cost causation. Initial comments by IXCs and large business customers assert other bases for analyzing universal service that are inferior to a usage-based approach.

Sprint argues for a form of "head tax" as the cost recovery mechanism. It justifies the shift to per line items arguing that the benefit of universal service accrues only from being

²⁴ Worldcom, p. 15.

²⁵ SBC, pp. 4, 14-15; TWT, pp. 3-4; Qwest, p. 9; TCA, p. 3; OPASTCO, p.6; NECA, pp- 4-5; EPIK, p. 3; WT, p. 4; USAC, pp. 16-17.

²⁶ Sprint, Attachment A.

connected to the network, rather than using the network. “Since universal service provides potential benefits to all customers, all customers should pay and pay equally.”²⁷ As we have pointed out numerous times to the Commission, just being connected has little value. Actual use is what makes the network valuable. Since we know the actual use that individuals and businesses make of the interLATA network, we do not have to settle for potential benefits to allocate responsibility for universal service costs.

One can also debate whether it is necessary or that Congress intended for all customers to pay equally. To the contrary, Congress said that “telecommunications services providers should contribute on an equitable basis, Sprint simply ignores the explicit language of the law. The idea that head taxes are the only efficient and equitable way to pay for public goods is also not consistent with general practice in this country. For the better part of a century progressive income taxes have been the primary means of funding federal spending.”²⁸

D. Means-testing is Not the Core of the Congressional Approach to the Universal Service Program

The large business customers present a different view of universal service. They claim that “under a revenue-based funding scheme, high volume customers effectively

²⁷ Sprint, p. 7.

²⁸ Sprint (p. 7) analogizes universal service to “public health and public defense” and asserts that all customers should pay equally. The most efficient method for achieving this is to have customers pay on a per line basis. This is the only method that ensures equal treatment among the end users who actually make up the public switched telephone network.

One would think that the recent debate over income tax reform would have reminded Sprint that we actually pay for public goods in a progressive manner in this society. We do not fund public defense with a head tax, we do so with income taxes. Not only is each additional dollar of income taxed, but also the income tax rates are higher for higher income households.

subsidize low-volume customers when the goal is to have high-*income* customers subsidize those at the low end of the economic spectrum.”²⁹

The universal service program is not defined as an income transfer program. Income-based subsidies are only a small part of the overall program as defined by Congress (the lifeline program).³⁰ Even here the intention is to use means testing to distribute benefits, not recover costs.

The Congressional intent to ensure that rural areas receive reasonably comparable services at reasonably comparable rates makes not reference to income-based criteria. Nor does the schools and libraries language. The large business users focus their attention entirely on section 254 (b)(1) of the Act, which requires that service be affordable³¹ completely ignoring the much broader and independent principles stated by Congress in the other subsections of section 254, which are not means tested.

Moreover, in Section 254 (k) Congress made it clear that it sought to protect a class of service (basic service) not a group of customers. Legislative language that sought to ensure that no more than a reasonable share of joint and common costs would fall on basic service³²

²⁹ Ad Hoc, p. 14.

³⁰ Section 254 (b)(3)

Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

³¹ Ad Hoc, p. 31.

³² Section 254 (k).

The Commission, with respect to interstate services, and the States, with respect to intrastate services, shall establish any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that service included in the definition of universal service bear no more

(and report language that contemplated an even smaller share),³³ underscores the broad view that Congress took of universal service. The effort by the large business users to actually impose means tests on all aspects of universal service or to impose a means-test mentality on cost recovery in an effort to increase fixed monthly charges that fall on residential customers are contrary to the express intention of the Act.

Having misdefined the fundamental nature of the universals service program, the large business users chastise the Commission for not finding facts in its Notice that it was not supposed to be looking for. The claim that “[a] revenue-based funding mechanism implicitly presupposes that there is some correlation between *income* and *interstate usage*, yet the Commission has cited no factual evidence that would support such a finding.”³⁴ In fact, in the recently concluded low volume proceeding,³⁵ wherein the question of the relationship between income and usage was properly before the Commission, Consumer Commenters demonstrated conclusively that there is such a relationship.

E. Per Line Charges Would Result in Higher Charges on Most Residential Customers than a Uniform Percentage of the Bill Charge.

The effort of high volume business users to claim that flat per line charges will benefit low volume users is ludicrous. The large volume users argue that a uniform percentage is

than a reasonable share of the joint and common costs of facilities used to provide those services.

³³ The House recedes to the Senate in this section, whose report language adds the parenthetical comment ((and may bear less than a reasonable share)), see Conference report, p. 129.

³⁴ Ad Hoc, p. 14.

³⁵ See the comments and reply comments of “Texas Office of Public Utility Counsel, Consumer Federation of America and Consumers Union,” *In the Matter of Low-Volume Long-Distance Users*, Federal Communications Commission CC Docket No. 99-249.

unfair to low volume users because they pay a higher rate per minute for their toll calls. The example given is to contrast low volume users who pay very high rates per minute, “as high as 30 cents,” to high volume users (like themselves) who pay a much lower rate per minute, as low as 5 cents per minute.” The large business commenters conclude that “Under a fixed percentage, revenue-based surcharge, the low-volume DDD user would be required to pay up to six times as much per minute in USF surcharges as the higher-volume block-of-time customer.”³⁶

The large business users focus on the rate, but not the total amount paid. A substantial number of residential consumers make no calls in a given month, so the rate does not matter.³⁷ In fact, under the large business user approach we would expect the universal service flat rate line charge to be over \$2.00 per month and the vast majority of residential customers would pay more than if the Commission adopted a uniform percentage mark-up.³⁸

³⁶ Ad Hoc, p. 16.

³⁷ Sprint, p. 15, states that “IXCs serve a significant number of zero-billers” so this example is quite relevant.

³⁸ There are few specific estimates of what the per line charge would be. Worldcom (p. 24) notes that the CECA report (referred to by the Commission in its NPRM) uses a figure of \$2.31 per line. Home, p. 3, gives a figure “as high as \$2.50 per line.”

If one simply does the math (divides the IXC share of current USF funds by the total number of line) the figure is well above \$2.00. Worldcom offers an arbitrary figure of \$1.00 for residential customers and proposes to get the rest from large business customers. Consumer Commenters view this offer as a loss leader or Trojan horse. Once the principle of flat per line charges is established on the basis of a “disproportionate” allocation of costs to business customers, we will begin the inevitable process of large business customers and IXCs complaining about the “distortion” that results. Subsequent proceedings will witness the steady increase in the allocation of costs onto the bottom of the residential ratepayer’s bill, as happened with the subscriber line charge. All of the costs will be shifted to the bottom of the bill on an undifferentiated per line basis. We prefer the principled position that costs should follow usage as the indicator of benefits.

F. Efficiency Justifications are Dubious at Best

The large commercial users start their efficiency argument on the basis of universal service costs as a non-traffic sensitive cost. Non-traffic sensitive costs, they argue should be recovered in non-traffic sensitive charges.

Unfortunately, as always, their cost causation analysis stops at the point where their interests are best served. They define the cost as a predominantly loop cost and seek to assign those costs to all loops on a uniform basis. They never ask whether loop and other network costs are driven by the demands of large commercial customers. Because the network is engineered to meet the needs of the most demanding users, who are typically large business customers, they account for a far larger share of network costs than their loop count indicates.

The large business users are equally arbitrary in describing why some costs should be passed through to consumers as bottom of the bill charges and others should not. For example, the large business users argue that “uncollectibles and administrative overhead costs are simply two of the many discrete costs of doing business that every commercial entity faces to some extent and must reflect generally in its prices.”³⁹ We see universal service costs as just one of many discrete costs of doing business that the IXC should reflect in their prices.

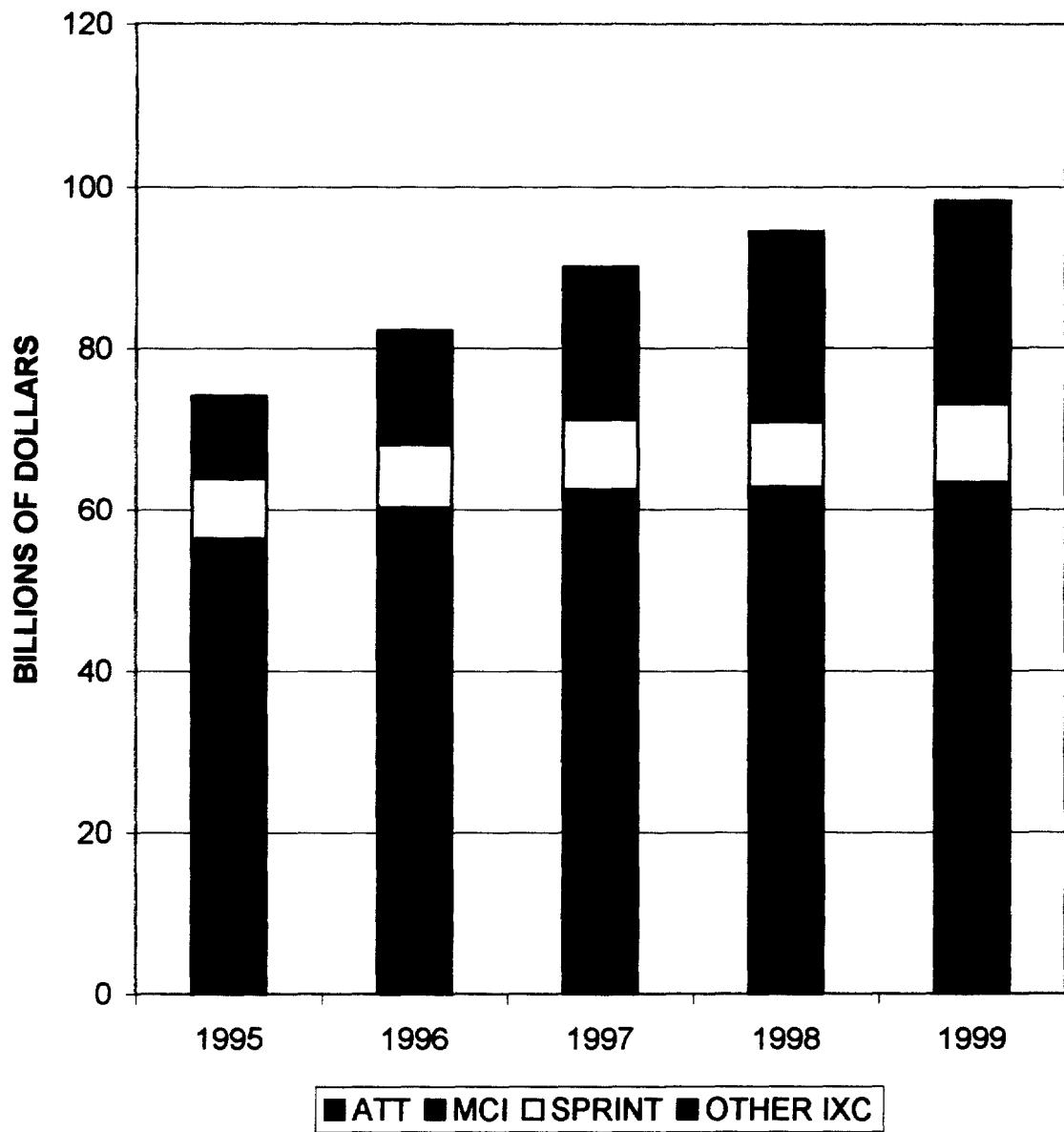
Finally, the large business users also seek to justify line items as demand side pricing which maximizes societal surplus by applying a form of Ramsey pricing. This approach seeks to maximize economic efficiency by charging consumers who have the least ability to shift demand (the fewest alternatives) the highest prices. It turns out that these are also the individuals with the least ability to pay.

There are numerous objections to Ramsey pricing that the Commission has heard in the past that need not be repeated here. Ramsey pricing rule when applied to intermediate goods and based on demand elasticities that have been determined in noncompetitive situations do not necessarily have the efficiency benefits claimed. Where demand elasticities are generally low, as they are in telecommunications, wealth transfers resulting from Ramsey pricing are large, relative to efficiency gains.

For the purposes of universal service funding we simply point out that Ad Hoc proposes a crude application of a Ramsey pricing principle (identifying access as a lower elasticity of demand service). In targeting end-users this approach runs counter to the clear intent of section 254 (b)(4), which required to the Commission to base its contribution mechanism on telecommunications service providers. In targeting basic monthly charges for maximum cost recovery, as the Ramsey principle does, runs counter to clear Congressional intent in section 254 (k) to minimize the burden of joint and common costs on basic service since adding fixed monthly charges to the bill to increase the cost of basic monthly service. Congress knew that the natural inclination of incumbent monopolists and large users is to shift joint and common costs onto the least elastic demand and it wrote the law to prevent that.

³⁹ Ad Hoc, p. 35.

EXHIBIT 1: LONG DISTANCE CARRIER TOLL REVENUES



SOURCE: Federal Communications Commission, *Statistics of Communications Common Carriers: 60th Anniversary edition, 1939-1999*, Table 1.4.